

OPEN SESSION AGENDA ITEM

50-3 MAY 2018

DATE: May 18, 2018

TO: Members, Board of Trustees

FROM: Donna S. Hershkowitz, Chief of Programs

SUBJECT: Adoption of Policy on Transfer of Excess Lawyer Assistance Program Funds to CSF, Pursuant to Bus. & Prof. Code §6140.9

EXECUTIVE SUMMARY

As part of its efforts to identify additional funds available to support the Client Security Fund (CSF), the Legislature amended Business and Professions Code §6140.9, effective January 1, 2018, to allow excess funds in the Lawyer Assistance Program (LAP) budget to be transferred to support the needs of the Client Security Fund. Specifically, the statute was amended to provide: "Any excess funds not needed to support the [LAP] program, including reserve funds, may be transferred to fund the Client Security Fund established pursuant to Section 6140.5, provided there are sufficient funds available to fully support the program." At its March 3, 2018, meeting, the LAP Oversight Committee (Committee) evaluated the condition of the LAP fund, and the statutory authorization to transfer excess LAP funds to support CSF, and developed a recommended transfer policy for the Board's consideration. This agenda item recommends a policy to implement that provision.

BACKGROUND

Business and Professions Code section 6140.9 provides that LAP is to be funded by an assessment as part of the annual licensing fee of \$10 per active attorney and \$5 for each inactive attorney. For 2018, the estimated revenue from these licensing fees is \$2.1 million. The Bar's 2018 budget projected the Lawyer Assistance Fund ending reserve balance in 2017 to be just under \$3.6 million. Based on expected revenue and currently budgeted expenditures for 2018, the Fund is projected to end 2018 with a reserve balance of just under \$3.5 million. Current Board policy establishes 30% of operating expenditures as the current maximum a fund should have, with 17% as the minimum. The 2018 projected year end reserve is 154% of operating expenditures.

DISCUSSION

Budgeted expenses for LAP for 2018 total \$2.2 million. This reflects an increase from the \$1.6 million in budgeted in 2017. The increase reflects budgeted expenses for staff resources necessary to implement the LAP Strategic Plan adopted in May 2017.

While historically annual LAP expenses have been less than annual revenue, in evaluating the extent of LAP funds that may be available for transfer, an examination of the current budgeted revenue and expenditures is insufficient. As noted above, the statute authorizes the transfer of funds “provided there are sufficient funds available to fully support the program.” The current LAP budget does not include projected costs for implementing key program goals. Among other things, in 2017, the LAP Oversight Committee adopted a Strategic Plan for LAP. In addition, the State Bar commissioned a review by an expert in the field, Patrick Krill, to make recommendations on how to improve the program. Additionally, there remain some outstanding recommendations from the 2016 Workforce Planning report that are pending full implementation.

Taking this into consideration, the Committee recommended that the Board adopt the following policy on transfer of excess LAP funds: to ensure there are sufficient funds available to fully support LAP, the amount available for transfer should be calculated by adding to the prior year’s reserve balance the budgeted revenues for the current year, and then subtracting the following: a) the amount of budget expenses and indirect costs; 2) the funds necessary to meet targets for growth and program enhancement and improvement, and to implement the current LAP Strategic Plan or any successor plan; and 3) an amount necessary to maintain the year end reserve balance at 25% of operating expenditures.

The Committee further recommended that the policy adopted by the Board specify that in determining the funds necessary to meet targets for growth and program enhancement and improvement, and implement the current LAP Strategic Plan or any successor plan, the Chief Financial Officer, or his or her designee, shall consult with the LAP Oversight Committee or its designee. After further consideration, staff recommends that the Board direct the Executive Director, or his or her designee to be responsible for this consultation.

The question of when it would be appropriate to implement that policy is complicated by the pending question currently under review of whether the LAP, and its clients, would be better served if a portion of LAP were either contracted out to private entities or spun off to its own private entity. This question will be part of the review of Board committees and commissions being conducted at the recommendation of the Governance in the Public Interest Taskforce (the “Appendix I” review). Those recommendations will be presented to the Board in September 2018. Should the decision be made that the best interests of the Bar and/or the program would be served by spinning off LAP, the calculus of how much of the excess reserves would be available for transfer to CSF would be exceedingly different. If the LAP were to operate on its own, it would likely need much of the existing reserves as startup capital. If the services are contracted out, or the LAP remains part of the Bar, implementation of the proposed policy would be appropriate.

To assist in understanding the impact of this policy, staff conducted a preliminary forecast of costs to implement the LAP Strategic Plan, as well as the recommendations from the 2017 Krill Report and the 2016 Workforce Planning report. Among other things, the forecast calculated costs for the development of printed educational and outreach materials, conducting outreach, including at law schools, conducting a market analysis of attorneys to determine their needs and how to disseminate information, and developing an online self-assessment to help identify mental health disorders and substance use issues for attorneys and law students.

Focusing on the importance of expanded outreach to the LAP Strategic Plan, the LAP Oversight Committee directed staff to include in the preliminary budget projection the costs to conduct outreach to all law schools by the end of the 2018 calendar year. (Staff had initially included projections for conducting outreach at 8 to 20 law schools.)

The preliminary projected costs for implementation of the recommendations of these important governing documents (including \$50,000 for a consultant to assist in the implementation of some of these costs), including outreach to all law schools, ranges from approximately \$190,000 to \$240,000. This preliminary projection does not estimate the costs of operating the program once the outreach efforts bear fruit (i.e., after the growth in the number of participants anticipated as a result of successful outreach efforts.).

In considering the timing for implementing that policy, the LAP Oversight Committee felt strongly that no funds should be transferred until after the Appendix I review is considered by the Board and a determination is made with respect to LAP's continued relationship with the State Bar of California, and the LAP is reasonably able to estimate the anticipated costs associated with targeted program growth, enhancement and modification. The Committee specifically recommends that the Board make no transfer until after December 31, 2020. The Committee believes strongly that transferring any funds before giving the program sufficient time to figure out the ongoing operational needs of the fully realized program would be contrary to the statutory direction of ensuring there remain "sufficient funds" for LAP, and could endanger the health of the program while we are in the process of trying to enhance and improve it. Recent developments which could impact the available resources include the addition of two items in AB 3249, the State Bar's licensing fee bill. The first provision in this legislation would redirect \$1 of every \$10 of the licensing fees that go to support LAP to a nonprofit entity engaged in substance abuse peer support. The second provision would amend Business and Professions Code section 6140.9 to expressly allow LAP funds to be used for treatment services for those who cannot afford to pay. These two provisions, if enacted, will have an impact on both the annual revenue and the annual expenses of LAP.

For the Board's information, after taking into account current budgeted revenue, expenditures, and estimated expenditures necessary to support the implementation of the LAP Strategic Plan, Krill report, and other recommendations for program growth and improvement (the \$190,000 - \$240,000 noted above), and leaving the fund with an appropriate level of reserves (25%), there is approximately \$2.6 million eligible for transfer to the Client Security Fund after application of the recommended policy.

In addition to the possible changes to the structure of the LAP and the fact that its current expenditures may not be representative of the ongoing costs of a fully enhanced program, the Board may wish to consider the points below in determining the proper timing for implementing this LAP reserve transfer policy.

Effective January 1, 2018, the Legislature provided express statutory authority to transfer excess funds from LAP to the CSF. This was done in conjunction with the addition of statutory language that expressly recognized the importance of the CSF to adequately protect the public and relieve or mitigate financial losses caused by the dishonest conduct of members of the State Bar. (See Business and Professions Code section 6140.56, directing the State Bar to conduct an analysis of the CSF and other State Bar expenditures to determine if other funds could be redirected to support the CSF.)

The 2018 Client Security Fund Report identified a number of options for consideration, including initiatives to provide additional resources to CSF, modification of executive and represented staff salaries, and one-time and on-going CSF fee increases ranging from \$5 to \$67 per licensed attorney. The Report found that the amount of nominal amount of outstanding requests for reimbursements totaled \$52.4 million, with \$23.4 million likely to paid, \$14.2 million of which is currently eligible for payment. In addition to that substantial one-time shortfall, the Report identified an on-going shortfall of \$1.8 million in excess of annual funding for CSF.

In discussing the then-draft of the 2018 Client Security Fund Report at its March 2018 meeting, the Board directed staff to report back on the possibility of redirecting excess LAP funds to CSF. This agenda item constitutes that report back.

The Assembly Judiciary Committee analysis of the State Bar's annual licensing fee legislation (AB 3249), for the May 8, 2018 committee hearing, considered the various options for increasing available CSF funds. The analysis concluded that in lieu of any options that would reduce the amount of reimbursement to applicants or place limitations on eligibility for CSF, "it is far preferable to consider ways to increase funds in the CSF. Possible methods proposed by the Bar include: . . . [t]ransferring surplus LAP funds o CSF, as specifically permitted in last year's SB 36. . . ."

With all of the above context in mind, and in contrast to the Committee's position, it may be prudent for the Board to decide to transfer a portion of the approximately \$2.6 million in available LAP funding to the CSF at this time; an amount ranging from \$250,000 to \$500,000, which equates to 35-70 additional 2018 payouts, may be appropriate.

FISCAL/PERSONNEL IMPACT

Because this policy is intended to transfer only "excess" funds, leaving "sufficient funds to fully support" LAP, although there is technically a fiscal impact, there should be no operational impact on LAP. The addition of these funds will allow CSF to pay out additional claims. In 2017, the average amount paid out to victims was just over \$7,000. At this rate, the infusion of \$2.6 million could allow payment on approximately 370 additional applications.

RULE AMENDMENTS

None

BOARD BOOK AMENDMENTS

None

STRATEGIC PLAN GOALS & OBJECTIVES

Goal: 2. Ensure a timely, fair, and appropriately resourced admissions, discipline, and regulatory system for the more than 250,000 lawyers licensed in California.

Objective: f. Support adequate funding of the Client Security Fund.

Goal: 3. Improve the fiscal and operational management of the State Bar, emphasizing integrity, transparency, accountability, and excellence.

Objective: h. As part of the annual budget development process, determine, consistent with Business and Professions Code section 6140.9, whether there are excess funds in the LAP fund which can be transferred to support the CSF.

RECOMMENDATION

It is recommended that the Board of Trustees approve the following resolution:

RESOLVED, that Section V of the Budget Policies and Procedures Manual be amended to include the following policy regarding the transfer of LAP reserves to support the Client Security Fund:

To ensure there are sufficient funds available to fully support LAP, annually, as part of the budget development process, the amount of LAP reserves available for transfer shall be calculated by adding to the prior year's reserve balance the budgeted revenues for the current year, and then subtracting the following: 1) the amount of budget expenses and indirect costs; 2) the funds necessary to meet targets for growth and program enhancement and improvement, and to implement the current LAP Strategic Plan or any successor plan; and 3) an amount necessary to maintain the year end reserve balance at 25% of operating expenditure.

In determining the funds necessary to meet targets for growth and program enhancement and improvement, and implement the current LAP Strategic Plan or any successor plan, the Executive Director, or his or her designee, shall consult with the LAP Oversight Committee or its designee.

ATTACHMENT(S) LIST

None